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COMMONWEALTH OF VIRGINIA

STATE CORPORATION COMMISSION

AT RICHMOND, DECEMBER 18, 2001

APPLICATION OF

COMMUNITY ELECTRIC COOPERATIVE

CASE NO. PUE000746

For approval of a functional
separation plan pursuant to
Virginia Code § 56-590

FINAL ORDER

On December 27, 2000, Community Electric Cooperative ("Community Electric" or the "Cooperative") filed an application for Commission approval of the Cooperative's plan for functional separation ("Plan") as required by the Virginia Electric Utility Restructuring Act ("the Act"), Chapter 23 of Title 56 of the Code of Virginia (§ 56-576 et seq.). The Act requires that the Commission complete its review of proposed plans of functional separation by January 1, 2002, and that transition to competition be implemented according to a timeline established by the Commission. Pursuant to an Order issued on March 30, 2001, in Case No. PUE000740, the Commission established January 1, 2004, as the deadline for the Cooperative and other electric cooperatives to provide full retail access for their customers.

The Commission promulgated rules¹ for functional separation as required by the Act. These Rules require the Cooperative to file a Plan that includes a cost of service study separating the Virginia jurisdictional operations into functions: generation, transmission, and distribution, subdivided by class and specifically identifying the costs associated with metering and billing. The Rules also require that the Plan include proposed unbundled rates, tariffs, and terms and conditions for service. Requests for waiver from the required submission of documents under the various sections of the Rules are also permitted.

In its application, the Cooperative stated that it is currently functionally separated. It does not own or control any generation or transmission facilities, nor does it own or control any affiliated entity that owns or controls generation or transmission facilities. Instead, Community Electric purchases all of its requirements for demand, energy, transmission and ancillary services through contracts with Old Dominion Electric Cooperative and Southeastern Power Administration. As such, Community Electric stated that it had no plans to divest itself of any generation assets, to create any new functionally separate entity, or to propose to transfer any functions, services, or employees to a functionally separate

¹ Commission's Regulations Governing the Functional Separation of Incumbent Electric Utilities under the Virginia Electric Utility Restructuring Act ("Rules"), 20 VAC 5-202-10 et seq., adopted in Case No. PUA000029.

entity or third party. The Cooperative filed a cost of service study, which included proposed unbundled rates to illustrate the Cooperative's rate unbundling. In its application, the Cooperative requested that the Commission waive the requirement of 20 VAC 5-202-40 B 8 of the Rules to file unbundled tariff rates and terms and conditions of service with the Cooperative's functional separation plan. The Cooperative also requested that the waiver extend until the conclusion of this proceeding so that it can finalize and submit such filings in compliance with the final order.

In an Order dated March 14, 2001, in this proceeding, the Commission directed the Cooperative to provide notice to the public and established a procedural schedule for the filing of comments or requests for hearing on Community Electric's application. In that Order, the Commission directed its Staff to investigate the application and file a Report detailing its findings and recommendations on or before June 7, 2001. The Commission also granted Community Electric's request for a waiver. However, the Commission required the Cooperative to file tariff terms and conditions of service in time for the Commission to consider them and to require notice, if necessary and appropriate, prior to the Cooperative's implementation of retail choice to its customers.

On June 7, 2001, Staff filed its Report wherein it recommended that the Commission approve Community Electric's

Plan with the adoption of certain modifications recommended by Staff. Specifically, Staff recommended that the Commission adopt the following: Staff's recommendation to consolidate the Cooperative's Generation and Transmission ("G&T") functions into one function;² Staff's adjustments to the Cooperative's per books cost of service study; Staff's allocations of expense and rate base to the G&T function; Staff's recommendation that the Commission direct the Cooperative to track the costs associated with G&T operations; and Staff's recommendation that the Commission direct Community Electric to provide tariff rates and terms and conditions of service in time for full consideration by the Commission.

On June 15, 2001, Community Electric filed its Response to the Staff Report. In its Response, the Cooperative stated that although it supports Staff's recommendation that the G&T functions be combined, it does not agree with Staff's recommendations pertaining to functional cost assignment. Community Electric requests that the Commission find that its administrative and general ("A&G") expenses and associated overheads are properly assignable to the distribution function because the rate paid by Community Electric to Old Dominion Electric Cooperative for power supply and transmission services

² Staff noted that the Cooperative does not anticipate providing transmission service to customers who shop for energy.

includes a component for A&G expenses. Community Electric argued that assigning its A&G and overheads to G&T would, in effect, add a second layer of such costs to the generation component. Further, Community Electric argued that in its role as the local distribution service provider, it is required by the Act to provide default generation service under its capped rates. According to Community Electric, supplying default generation services provides a benefit available for all consumers on Community Electric's distribution system, including those consumers who may choose an alternative power supplier. Community Electric further stated that the responsibility bestowed on it to provide default service is a function of its role as the distribution utility. Thus, the Cooperative urged the Commission to reject Staff's proposal to assign A&G costs to the G&T functions.

With regard to Staff's recommendation concerning the allocation of certain integrated load management system costs, those relating to system control and data acquisition, Community Electric took issue with Staff's allocation of such costs to the G&T function. Community Electric maintained that such costs should be allocated to the Distribution function.

Although Community Electric agreed that a portion of property tax should be allocated to G&T, it took issue with the proper factor that should be used for such allocation. Community Electric asserted that A&G property tax should be

allocated using a General Plant factor rather than an A&G labor factor.

On June 27, 2001, Staff filed a motion requesting leave to file reply with an attached Reply. In response to Community Electric's assertion that certain A&G costs should be allocated to Distribution, the Staff maintained its position that if these costs are shifted to Distribution, rates established for Distribution will subsidize those of G&T, contrary to § 56-590 D of the Code of Virginia, which requires the Commission to set rates that will not result in cost shifting or cross-subsidies between functional units. The Staff did not take issue with Community Electric's position that certain integrated load management system costs relating to SCADA should be allocated to the Cooperative's Distribution function rather than the G&T function. Staff did not address the issue of the proper factor for use in allocating property tax to G&T.

On July 2, 2001, Community Electric filed a motion requesting leave to file reply with a Reply attached, and filed a motion to deny Staff's motion requesting leave to file reply. In its Reply, the Cooperative maintained that failure to attribute additional A&G expenses to the generation function does not result in cost shifting or cross-subsidization of functionally separate units. In addition, Community Electric urged the Commission to consider its unique statutory obligation to provide default services in Virginia.

NOW THE COMMISSION, having considered the Cooperative's application, Staff's Report, the subsequent pleadings, and applicable law, is of the opinion and finds that the application should be approved, subject to the modifications detailed herein. We will grant Staff's motion requesting leave to file reply and also grant Community Electric's motion requesting leave to file reply.

With respect to the issue of the proper allocation of A&G costs supporting the procurement of wholesale power, we find that the Commission has an obligation pursuant to § 56-590 D of the Code of Virginia to see that no cross-subsidies occur. The function causing the cost should be allocated such costs. A&G costs associated with the procurement of wholesale power support the G&T function, and as such, should not be allocated to the Distribution function. We will, therefore, accept Staff's adjustment allocating certain A&G costs associated with obtaining wholesale power to the Cooperative's G&T function.

There are two ways that a cooperative may recover A&G costs associated with the procurement of wholesale power. If a customer remains with the cooperative, the cooperative will recover such costs from the customer. If the customer leaves the cooperative, and the embedded cost of generation exceeds the market, the cooperative will have the opportunity to recover the cost through the wires charge.

We will accept Community Electric's position with respect to the allocation of certain integrated load management system costs relating to SCADA and allocate such costs to the Distribution function. We will also accept the Cooperative's position with respect to the proper allocation factor for property taxes and will use a General Plant Factor in allocating such taxes to G&T.

We find that G&T costs, as defined in this Order, should be tracked prospectively by the Cooperative in order to ensure accurate functional allocations in any future proceedings before the Commission. We also direct the Cooperative to begin tracking the incremental costs associated with billing and collection costs, as well as the activities that give rise to the customer service and legal and regulatory costs.

Finally, in its cost of service study, Community Electric discusses the impact of its monthly fuel adjustment factor in relation to the determination of the market price for generation and the wires charge. It is the Cooperative's position that fuel adjustments can be applied monthly without violating §§ 56-582 and 56-583 of the Code of Virginia. We are not persuaded by the Cooperative's argument on this point. However, because it is not necessary that we resolve this issue prior to January 1, 2002, we will defer our consideration of it until next year. In the interim, we direct the Staff to (i) consult with Community Electric, the other electric cooperatives, and any interested

parties on this issue and (ii) submit a written recommendation to the Commission on or before March 1, 2002, on whether we should implement an annual fuel factor adjustment for the cooperatives in lieu of the current fluctuating monthly fuel charge.

Accordingly, IT IS ORDERED THAT:

(1) Staff's motion requesting leave to file reply is hereby granted.

(2) Community Electric's motion requesting leave to file reply is hereby granted.

(3) Community Electric's Plan for functional separation pursuant to the Virginia Electric Utility Restructuring Act is hereby approved, subject to the modifications discussed herein.

(4) On or before March 1, 2002, the Staff shall submit a written recommendation to the Commission on whether we should transition to an annual fuel factor adjustment for the cooperatives from the current fluctuating monthly fuel charge, and if so, how such a transition should occur.

(5) Community Electric shall provide tariffs and terms and conditions of service to the Division of Energy Regulation that conform to this Order and all applicable Commission Rules and Regulations one hundred fifty (150) days prior to its implementation of retail choice.

(6) This case is hereby dismissed, and the papers shall be placed in the file for ended causes.